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# China Changes the Global Oil Game

By Jonathan Broder, CQ Staff

Over the past two decades, China's enormous economic growth has transformed it from the largest oil exporter in East Asia to the world's second-largest oil importer, after the United States. And in its relentless quest for energy sources, China is also changing the global oil market.

China's state-owned oil companies have signed bilateral oil and gas deals with some 30 countries, ranging from traditional suppliers in the Middle East to unconventional producers in Central Asia, Africa, Venezuela and Canada.

And to ensure long-term energy security, China has decided to pay producer nations big premiums for control of those energy reserves. That willingness was illustrated by its unsuccessful $18.5 billion bid for Unocal Corp. — $1.5 billion more than the final offer by Chevron Corp., the next closest bidder. China can afford to pay such premiums because it is sitting on $610 billion in foreign currency reserves, according to the CIA.

CORNERING THE MARKET: China's state-owned oil companies have bilateral oil and gas deals with about 30 countries. (GETTY IMAGES / CHINA PHOTOS)

Like other commodities, oil has been bought and sold for decades in international markets in what energy experts call "the bathtub approach." Under this system, companies and states draw what they need from available global supplies and pay for it at international markets such as the New York Mercantile Exchange and the International Petroleum Exchange in London.

But China's success in securing dedicated reserves from certain producer nations "will change the game for countries that are playing on the fungible market," says Frank A. Verrastro, director of the energy program at the Center for International and Strategic Studies, a nonpartisan Washington think tank.

For those players, the removal of China-dedicated oil from the world market means overall supplies could be that much lower, guaranteeing that today's already high prices will continue rising, many energy experts say. Of the 3.5 million barrels of oil that China imports each day, about 11 percent comes from these bilateral deals, the Energy Department says. With China cutting more such deals, experts predict, that percentage will rise in the years ahead.

In fact, China has turned to the United States' biggest oil suppliers in the Western Hemisphere to help feed its energy needs. Last December, it secured agreements to explore for oil and natural gas in Venezuela. To facilitate the shipment of that oil back home, it also is helping build a pipeline to the Colombian coast on the Pacific.

Venezuela's leftist President Hugo Chavez, an outspoken critic of U.S. policies in Central and South America, has described the deal as a way to reduce his country's dependence on the U.S. market. "We have been producing and exporting oil for more than 100 years, but these have been 100 years of dependence on the United States," he said after the deal with China was signed. "Now we are free and we place this oil at the disposal of the great Chinese fatherland."

In response to Hurricane Katrina, however, Chavez has pledged to maintain — at least for now — Venezuelan oil shipments to the United States, although he has periodically threatened to cut off trade between the countries.

China also has sought to leverage strained U.S.-Canadian trade relations over lumber and cattle to its energy advantage. In June, China Petrochemical Corp, one of the largest state-owned energy companies, bought a 40 percent stake in Alberta's $3.6 billion oil sands project, which aims to produce light crude from the province's large tar pits. China is also seeking to buy a 49 percent share of a $2.5 billion pipeline to carry Alberta's oil to Canada's west coast for export to China, California and other markets.

Gal Luft, executive director of the Institute for the Analysis of Global Security, notes that in some producer countries, doing business with China is a way to send a political message to the United States. "Selling oil to China is a way of showing us the finger and saying that the United States cannot take them for granted," he says.

But with Venezuela and Canada together supplying close to a third of U.S. oil imports, experts say the United States can ill afford to lose portions of the crude oil from these two important suppliers.

"Every barrel of oil that goes exclusively to China is one that the United States has to find on the tightening global market," said Alan S. Hegburg, an energy expert at the Scowcroft Group, a Washington-based international business consultancy.

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